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C O N F I D E N T I A L SECTION 01 OF 03 TAIPEI 000378

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TAGS: [ECON](#) [EINV](#) [EFIN](#) [PREL](#) [TW](#) [CH](#)
SUBJECT: BIGGEST TAIWAN INVESTOR IN PRC SUSPICIOUS OF
DEMOCRACY

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Classified By: AIT Director Stephen M. Young, Reason 1.4 d

¶1. (C) Summary: Hon Hai Group Chairman Terry Gou expressed to the Director on February 14 reservations about the effects of democracy on economic performance, criticizing corruption in village-level elections in China and praising China's Communist Party leaders as concerned primarily with the interests of China's people. Gou also disparaged democracy in India and excessive regulation in the United States. When Gou said that 99 percent of people in China believe the U.S. wants to prevent reunification of Taiwan and the Mainland, the Director disabused him of the notion, saying our only concern is that no settlement be forced upon the people of Taiwan. A greater challenge will be to convince Taiwan investors like Gou to use their influence in the PRC to encourage democratic reform. End summary.

¶2. (C) AIT Director Young met with Terry Gou, the chairman of Hon Hai Group, on February 14, 2007, to discuss prospects for Taiwan's economy and cross-Strait relations. Gou started Hon Hai in 1974 with US\$2,500 and 10 employees. Today it is Taiwan's largest firm with revenue of over NT\$1.2 trillion (US\$37 billion) in 2006. It is also the world's largest contract manufacturer of IT hardware, producing a wide range of electronics goods primarily for U.S. and other foreign brand name companies. Its products include personal computers, networking equipment, digital cameras, video game consoles, and most recently the Apple iPhone. Hon Hai is Taiwan's largest investor in the PRC. In addition, it is the largest exporter in the PRC among all firms, local and foreign.

Suspicious of Democracy - China Not Ready,...

¶3. (C) Gou expressed to the Director reservations about the effects of democracy on economic performance. Gou

described democratic elections at the village level in China as contests among the candidates to see who can attract the most investment. He said vote buying and other corruption were common in the election process and complained that Chinese voters are not educated enough to know what campaign practices are illegal. Gou argued that corruption among senior leaders in China is the exception. He believes China's Communist Party leaders are generally sincere in their desire to improve the standard of living of China's people. He cited Liaoning Province Party Secretary Li Keqiang as an example. Gou noted that he signed an agreement the previous week to build factories in Liaoning that will make auto parts and printed circuit boards.

14. (C) The Director commented on Taiwan's positive influence on the PRC as a democracy that holds elected leaders accountable. He also noted the potential for Taiwan investors to have a positive impact on PRC society beyond fueling further economic growth. Gou agreed, pointing out that Taiwan had absorbed influences from Japan during the colonial period and more recently from the United States in large part through strong ties between U.S. and Taiwan companies. He acknowledged the potential for this "melting pot" effect to occur between Taiwan and China through deeper economic integration. However, Gou questioned the motives of U.S. cross-strait policies. He claimed that 99 percent of people in China believed the United States wants to prevent reunification of Taiwan and the PRC. The Director vigorously affirmed that the United States' goal is to promote a peaceful resolution of the cross-strait conflict, and that any agreement reflects the free will of the people of Taiwan.

"Too Much Equality" in India,...

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15. (C) When the Director noted the positive example of democratic India's dynamic economy, Gou challenged the notion that democracy had contributed to its recent growth. He explained that Hon Hai had a cellular phone factory near Chennai and he had been very optimistic about India's potential as an investment destination a year ago. However, now he believes there is "too much equality" in India. He related the story of a trip to Hon Hai's Chennai facility that had taken an hour and forty minutes by car from the city center. At the time, there was a new highway under construction that was expected to cut the trip to under an hour. Gou said that when he returned a year later, after construction of the highway was complete, the trip took two hours because the new highway was clogged with bicycles and cows. He complained that democracy made everyone feel entitled to use the new highway.

And Too Many Lawyers in the U.S.

16. (C) Gou also made critical observations on the U.S. economy. The United States, he said, has too many lawyers. He complained that excessive regulation made it difficult to list on U.S. stock exchanges. Gou predicted that in ten years, the combined value of the Hong Kong, Taipei and Shanghai stock exchanges would exceed the combined value of the New York and Tokyo stock exchanges. As he described his investment plans for the auto parts industry, Gou also said that General Motors and Ford had lost competitiveness because of poor management. He commented that their management style compared poorly with the firms he worked with in Silicon Valley. Similarly, Gou criticized management at Japan's large firms, remarking that the second and third generation of leadership in the firms thinks too much like government officials.

Moving Out of the Pearl River Delta

17. (C) Gou described ambitious plans to expand investment in new locations outside of Hon Hai's large base in Guangdong Province, China. He is particularly optimistic about prospects in Vietnam and has large-scale investment planned there. Gou said labor is cheaper in Vietnam than Guangdong but still of good quality. He said he can train the work force he needs there in a few months. Hon Hai plans to bring 2,000 to 3,000 Vietnam employees to its Shenzhen facility for training. Eventually, Gou said, Hon Hai plans to reduce by 40 percent its 450,000-employee workforce in Shenzhen and replace it with workers in Vietnam. In addition to his Liaoning Province plans, Gou mentioned investment plans in Shanxi Province (the birthplace of Gou's father). He dismissed investment potential in the other BRIC countries (Brazil, Russia, and India). Noting that the group already has a factory in Brazil, Gou expressed little interest in expanding there. Hon Hai had considered moving its plant in the Czech Republic to St. Petersburg, Russia, but had abandoned that plan.

Taiwan's Economic Future

18. (C) The Director asked Gou about what industries showed promise for Taiwan's economic future. Gou said the semiconductor industry will continue to be an important economic driver because the product is small, light and easy to ship. However, Gou expects other Taiwan firms to continue moving manufacturing operations out of Taiwan, even as they keep research, development and design operations on the island. He pointed out that

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Hon Hai owns a thin-film transistor liquid crystal display (TFT-LCD) manufacturing affiliate named Innolux in Miaoli County, but Gou believes that even capital-intensive TFT-LCD manufacturing operations will eventually move out of Taiwan. He highlighted digital content as an area of future growth, commenting that providing content is a natural area of expansion for IT hardware manufacturers like Hon Hai. Gou described his investment in a film production company in Shanxi as an example. He noted that Zhang Yimou, the Chinese director, is one of his partners in the venture. Biotechnology holds less promise for Taiwan, Gou said. He believes China has a stronger advantage in this field.

Comment - Taishang as Agent for Change?

19. (C) Hon Hai's Terry Gou is a prime example of a Taiwan businessman who has staked his future on China. The son of Mainland-born parents, Gou already had strong ties to China, but his business relationships have consolidated his affinity for his ancestral homeland. As China's largest exporter, his economic influence on the Mainland is undeniable. The geographic reach of his PRC operations is also impressive. As he expands into the film industry, Terry Gou will have an enhanced ability to influence the culture of greater China as well. The opportunity to disabuse him of the notion that the U.S. seeks to keep Taiwan away from China was a welcome one. A greater challenge will be to convince Taiwan investors like Gou to use their influence in the PRC to encourage democratic reform.

YOUNG